

regulations contained amendments to the regulations previously proposed under sections 6042 and 6044.

In the Rules and Regulations section of this issue of the Federal Register, the IRS is issuing final regulations relating to backup withholding that were proposed in INTL-52-86 and IA-224-82. Those final regulations do not include proposed §§ 1.6042-5 and 1.6044-6. Further, when the IRS issues additional final regulations that were proposed under INTL-52-86, those additional final regulations will not include proposed §§ 1.6042-5 and 1.6044-6. Accordingly, this document withdraws those proposed regulations sections. See §§ 1.6042-4 and 1.6044-5 of the final regulations for substantive rules proposed under the withdrawn sections.

#### List of Subjects 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

#### *Withdrawal of Portion of Notice of Proposed Rulemaking*

Accordingly, under the authority of 26 U.S.C. 7805, proposed §§ 1.6042-5 and 1.6044-6 that were published in the Federal Register on February 29, 1988 (53 FR 5991) and amended in the Federal Register on September 27, 1990 (55 FR 39427) are withdrawn.

Margaret Milner Richardson,  
Commissioner of Internal Revenue  
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#### 26 CFR Part 1

[EE-53-95]

RIN 1545-AT95

#### Requirements for Tax Exempt Section 501(c)(5) Organizations

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Notice of Proposed Rulemaking.

**SUMMARY:** This document contains proposed regulations clarifying certain requirements of section 501(c)(5). The requirements are being clarified to provide needed guidance to organizations as to the requirements an organization must meet in order to be exempt from tax as an organization described in section 501(c)(5).

**DATES:** Written comments and requests for a public hearing must be received by March 20, 1996.

**ADDRESSES:** Send submissions to: CC:DOM:CORP:T:R (EE-53-95), room 5228, Internal Revenue Service, POB

7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:T:R (EE-53-95), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC.

**FOR FURTHER INFORMATION CONTACT:** Robin Ehrenberg, (202) 622-6080 (not a toll-free number).

#### **SUPPLEMENTARY INFORMATION:**

##### Background

This notice of proposed rulemaking clarifies the scope of the exemption provided in section 501(c)(5) of the Internal Revenue Code for labor, agricultural and horticultural organizations.

An income tax exemption for labor organizations was first provided in the Corporation Excise Tax Act of 1909, Public Law No. 61-5, 36 Stat. 11, 112-118, and has been in effect continuously since that time. A labor organization is an entity that is organized "to protect and promote the interests of labor." *Portland Cooperative Labor Temple Association v. Commissioner*, 39 B.T.A. 450 (1939), acq., 1939-1 C.B. 28. The principal purpose of the organization must be to better the working conditions of people engaged in a common pursuit. See, *Treas. Reg. § 1.501(c)(5)-1*. Organizations meeting this requirement have traditionally engaged in collective action directed toward the workers' common objective of improving working conditions. They include labor unions that negotiate with employers on behalf of workers for improved wages, fringe benefits, hours and similar working conditions, and certain union-controlled organizations, like strike funds, that provide benefits to workers that enhance the union's ability to bargain effectively. See *Rev. Rul. 67-7* (1967-1 C.B. 137). They do not include strike funds that provide income to union members but are not controlled by unions. See *Rev. Rul. 76-420* (1976-2 C.B. 153). Such an organization will not pay the strike benefits "with the objective of bettering conditions of employment, but by reason of its contractual agreements with the workers."

Labor organizations may also meet the requirements of section 501(c)(5) by providing benefits that directly improve working conditions or compensate for unpredictable hazards that interrupt work. Examples of such benefits include operating a dispatch hall to match union members with work assignments and providing industry stewards who represent employees with grievances

against management. See *Rev. Rul. 75-473* (1975-2 C.B. 213); *Rev. Rul. 77-5* (1977-1 C.B. 148). On the other hand, managing saving and investment plans for workers, including retirement plans, does not bear directly on working conditions. See *Rev. Rul. 77-46* (1977-1 C.B. 147). Accordingly, section 501(c)(5) has not been applied to organizations that manage retirement savings plans as their principal activity.

Nevertheless, in *Morganbesser v. United States*, 984 F.2d 560 (2d Cir. 1993), the court held that a trust managing a pension benefit plan pursuant to a collective bargaining agreement qualified as a labor organization described in section 501(c)(5). The IRS and the Treasury Department believe that this decision is contrary to existing law, and the IRS is issuing an action on decision reflecting its view that the *Morganbesser* court erred in its holding. These proposed regulations are a clarification of the existing legal standard.

Like labor organizations, agricultural and horticultural organizations must also better the conditions of those engaged in a common pursuit in order to be described in section 501(c)(5). See § 1.501(c)(5)-1. There is no authority indicating that the law is to be interpreted differently for agricultural and horticultural organizations than for labor organizations. Accordingly, the proposed regulations clarify the law as it applies to all section 501(c)(5) organizations.

Certain organizations have taken the position in refund actions that they are labor organizations described in section 501(c)(5) even though their principal activity was to manage retirement savings plans for workers. In addition, some such foreign organizations have claimed exemption from withholding on dividend, interest and similar income that they have earned. The IRS will continue to oppose these claims for refund and exemption from withholding.

A health plan is not a retirement savings plan. Thus, the IRS will continue to follow *Rev. Rul. 62-17* (1962-1 C.B. 87) (regarding a labor organization providing health benefits) even in circumstances where a majority of the organization's members are retired. Furthermore, the IRS will continue to recognize that negotiating the terms of a retirement plan and other postretirement benefits and designating one or more representatives to the board of a multiemployer pension trust are proper activities for a labor organization. The proposed regulations are not intended to apply to or affect

any other provision of federal law, including provisions of the Employee Retirement Income Security Act of 1974 (ERISA) administered by the Secretary of Labor.

#### Explanation of Provisions

The proposed regulations add a new paragraph to § 1.501(c)(5)-1 providing that an organization is not an organization within the meaning of section 501(c)(5) if the organization's principal activity is to manage savings or investment plans or programs, including retirement savings plans.

#### Proposed Effective Date

These regulations are proposed to be effective December 21, 1995.

#### Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

#### Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be available for public inspection and copying. A public hearing may be scheduled if requested in writing by a person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the hearing will be published in the Federal Register.

#### Drafting Information

The principal author of these regulations is Robin Ehrenberg, Office of Associate Chief Counsel (Employee Benefits and Exempt Organizations). However, other personnel from the IRS and Treasury Department participated in their development.

#### List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

#### Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

#### PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 \* \* \*

Par. 2. Section 1.501(c)(5)-1 is amended by:

1. Redesignating paragraph (b) as paragraph (c).
2. Adding a new paragraph (b) to read as follows:

#### § 1.501(c)(5)-1 Labor, agricultural, and horticultural organizations.

\* \* \* \* \*

(b)(1) An organization is not an organization described in section 501(c)(5) if the principal activity of the organization is to receive, hold, invest, disburse, or otherwise manage funds associated with savings or investment plans or programs, including pension or other retirement savings plans or programs.

(2) *Example.* Trust A is organized in accordance with a collective bargaining agreement between a labor union and multiple employers. Representatives of both the employers and the union serve as trustees. Trust A receives funds from the employers who are subject to the agreement, invests the funds and uses the funds and accumulated earnings to pay pension benefits to union members as specified in the agreement. It also provides information to union members about their retirement benefits and assists them with administrative tasks associated with the benefits. Most of Trust A's activities are devoted to these functions. From time to time, Trust A also participates in the renegotiation of the collective bargaining agreement. Because Trust A's principal activity is to manage funds associated with a pension plan, it is not an organization described in section 501(c)(5).

\* \* \* \* \*

Margaret Milner Richardson,

*Commissioner of Internal Revenue.*

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#### 26 CFR Part 1

[EE-20-95]

RIN 1545-AT47

#### Effect of the Family and Medical Leave Act on the Operation of Cafeteria Plans

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** This document contains proposed regulations relating to cafeteria plans that reflect changes made by the Family and Medical Leave Act of 1993. The proposed regulations provide the public with guidance needed to comply with the Act and affect employees who participate in cafeteria plans.

**DATES:** Written comments and requests for a public hearing must be received by March 20, 1996.

**ADDRESSES:** Send submissions to: CC:DOM:CORP:R (EE-20-95), room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R (EE-20-95), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC.

**FOR FURTHER INFORMATION CONTACT:** Concerning the regulations, Catherine Fuller, (202) 622-6080; concerning submissions and the hearing, Mike Slaughter, (202) 622-8452 (not toll-free numbers).

#### SUPPLEMENTARY INFORMATION:

##### Background

This document contains proposed additions to the Income Tax Regulations (26 CFR Part 1) under section 125 of the Internal Revenue Code of 1986 (Code). These additions are proposed to conform the regulations to the Family and Medical Leave Act of 1993 (FMLA), Public Law 103-3. FMLA imposes certain requirements on employers regarding coverage, including family coverage, under group health plans for employees taking FMLA leave, and regarding the restoration of benefits to employees who return from FMLA leave. This notice of proposed rulemaking addresses a number of the principle questions that have been raised about how these FMLA requirements affect the operation of cafeteria plans (including flexible spending arrangements) maintained under section 125 of the Code. The rules in this notice of proposed rulemaking supplement the proposed Income Tax Regulations under section 125 of the Code. Except as otherwise provided in this notice of proposed rulemaking, all of the existing rules governing cafeteria plans, including the nondiscrimination rules, continue to apply.

The requirements pertaining to FMLA leave, including the employer's obligation to maintain coverage under a group health plan during FMLA leave and to restore benefits upon return from FMLA leave, are established by FMLA,